

COMMONWEALTH OF KENTUCKY  
BEFORE THE UTILITY REGULATORY COMMISSION

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In the Matter of:

NOTICE OF ADJUSTMENT OF RATES OF )	
CEDAR CREEK SEWER COMPANY, INC. )	CASE NO. 7931
D/B/A CEDAR LAKE PARK SEWER )	
SYSTEM TO BECOME EFFECTIVE ON )	
AUGUST 22, 1980 )	

O R D E R

On July 31, 1980, Cedar Creek Sewer Company, Inc., (hereinafter Applicant or the Company) filed with this Commission its notice of a general adjustment of rates to become effective on August 22, 1980. The proposed adjustment would produce additional annual revenues of approximately \$28,200, an increase of 88.1% based on test year revenues. Applicant stated that the rate adjustment was necessary in order for the Company to adequately render service and maintain its financial integrity.

On August 1, 1980, the Commission issued an Order which suspended the proposed rate increase for a period of five months, or until January 22, 1981. On August 13, 1980, the Commission issued an additional Order directing Applicant to provide statutory notice of the pending rate increase and the scheduled hearing, set for October 9, 1980, to its consumers.

On August 20, 1980, the Division of Consumer Intervention in the Office of the Attorney General filed a motion to intervene in this proceeding which was sustained.

The hearing was conducted as scheduled at the Commission's offices in Frankfort, Kentucky.

COMMENTARY

Cedar Creek Sewer Company, Inc., is a privately-owned sewage treatment system serving 394 customers in Jefferson County, Kentucky. Applicant serves customers in the Cedar Lake Park Subdivision and the Casa Landa Subdivision, both in Jefferson County.

### TEST PERIOD

Applicant proposed and the Commission has accepted the twelve months ending April 30, 1980, as the test period for the purpose of determining the reasonableness of the proposed rates. In utilizing the historic test period the Commission has given full consideration to known and measurable changes where appropriate.

### REVENUE REQUIREMENTS

Applicant proposed several pro-forma adjustments to expenses in Exhibit C of its application. The Commission is of the opinion that the adjustments are generally proper and accepted for rate-making purposes with the following exceptions:

1. The adjustments to Miscellaneous Supplies and Chemical Supplies of \$73 and \$155, respectfully, are not properly supported as they are based on estimated increases in costs over a three year period. The Commission finds that these adjustments are without merit and thereby are not accepted for rate-making purposes.

2. The proposed adjustments of \$400 for engineering fees resulting from these proceedings and \$150 for recurring engineering fees should not be included herein. The Commission is of the opinion that the services provided in these areas by the Company's president are a part of his duties as president for which he receives an annual fee of \$1,800.

3. Actual repairs and Maintenance Expense included in the test year, per Applicant's books, amounted to \$4,940. The Commission, after reviewing the expenditures involved, is of the opinion that Applicant erroneously charged a number of items to expense which, based on their future value to the Company, should have been capitalized. Based on the reclassification of these items, the Commission has made an adjustment to reduce Applicant's Repairs and Maintenance Expense for the test year by \$829. Furthermore, the Commission does not agree with the use of the annual percentage method with which Applicant has made the pro-forma adjustment to this account; however, the Commission has taken into consideration

the increased labor and mileage charges of Applicant's service company, which became effective October 1, 1980, and finds the adjustment of \$741 to be acceptable.

4. Sewer Repairs Expense for the test year totaled \$2,213 per Applicant's books. The Commission feels that the expenditure of \$2,150 for the replacement of sixty (60) feet of main was erroneously expensed and that it should have been capitalized. The Commission, therefore, has reduced the test year expense for sewer repairs by \$2,150 to \$63. The Commission also does not accept the pro-forma adjustment, based on annual percentage increases, of \$332 thereby resulting in a provision for annual Sewer Repairs Expense equal to the adjusted test year expense of \$63.

5. For rate-making purposes, the Commission has adjusted Depreciation Expense to reflect the capitalization of the \$829 and the \$2,150 erroneously included by the Company in Repairs and Maintenance Expense and Sewer Repairs Expense, respectively. This results in an increase of \$137 in Depreciation Expense. The Commission has calculated this adjustment using service lives of ten (10) years and forty (40) years respectively and the straight-line method of depreciation.

6. Applicant had, during the test year, interest expense of \$5,552, on Long-Term Debt. The related debt obligation results from the Applicant's purchase of its common stock as treasury stock. The Commission is of the opinion that this was not an arms-length transaction but a transaction consummated only because of the mutual ownership of Applicant and the seller of the stock, Cogan Company, Inc. It is obvious to the Commission that this is a transaction set up for the benefit of the mutual owner and for the purpose of taking advantage of all possible tax benefits to the Applicant. While recording the transaction in this manner is both legal and proper for general accounting and tax purposes, the effect would be to require Applicant's consumers to pay the interest cost on the debt. Therefore, the Commission has adjusted operating expenses by \$5,552 to reflect the exclusion of this expense for the purpose of determining rates.

The effect of these adjustments on Net Income is as follows:

	<u>Test Year</u>	<u>Pro-forma Adjustments</u>	<u>Adjusted Test Year</u>
Operating Revenues	\$ 31,996	\$ -0-	\$ 31,996
Operating Expenses	<u>43,309</u>	<u>1,531</u>	<u>44,840</u>
Operating Income	<u>\$(11,313)</u>	<u>\$(1,531)</u>	<u>\$(12,844)</u>
Interest Income	1,118	(638)	480
Interest Expense	<u>5,552</u>	<u>(5,552)</u>	<u>-0-</u>
Net Income	<u>\$(15,747)</u>	<u>\$ 3,383</u>	<u>\$(12,364)</u>

The Commission is of the opinion that an operating ratio <sup>(1)</sup> of .88 will be adequate to allow Applicant to pay its operating expenses found reasonable for rate-making purposes. Based on this operating ratio Applicant's operating revenues should be \$50,955 which will require additional revenue of \$18,959.

#### RATES

The Commission has determined, in this matter, that due to current economic conditions and the relationship of those conditions to the housing industry that Applicant's rates should be based on test year customers rather than customers projected three years into the future. Therefore, the rates set out in Appendix "A" will produce gross annual revenue of \$49,691, based on test year-end customers. This revenue, combined with Applicant's other operating revenue will provide total operating revenue of \$50,955.

#### SUMMARY

The Commission, after consideration of the evidence of record and being fully advised, is of the opinion and so finds that the rates set out in Appendix "A", attached hereto and made a part hereof, will produce gross annual revenues of \$50,955 and are the fair, just, and reasonable rates for Applicant.

The Commission further finds that the rates proposed by the Applicant are unfair, unjust, and unreasonable in that they produce revenue in excess of that deemed reasonable herein and should be denied.

<sup>(1)</sup> 
$$\text{Operating Ratio} = \frac{\text{Operating Expenses} + \text{Depreciation} + \text{Taxes}}{\text{Gross Revenues}}$$

IT IS THEREFORE ORDERED, that the rates set out in Appendix "A", attached hereto and made a part hereof, are approved for service on and after the date of this Order.

IT IS FURTHER ORDERED, that the rates proposed by Cedar Creek Sewer Company are unfair, unjust, and unreasonable in that they produce revenue in excess of that deemed reasonable herein and are hereby denied.

IT IS FURTHER ORDERED, that Cedar Creek Sewer Company shall file with this Commission within thirty (30) days from the date of this Order its revised tariff sheets setting out the rates approved herein.

Done at Frankfort, Kentucky, this 18th day of December, 1980.

UTILITY REGULATORY COMMISSION

Did not participate

Chairman

John H. G. Mann

Vice Chairman

Mary Kay Eiken

Commissioner

ATTEST:

Secretary

APPENDIX "A"

APPENDIX TO AN ORDER OF THE UTILITY REGULATORY  
COMMISSION IN CASE NO. 7931 DATED DECEMBER 18,  
1980.

The following rates are prescribed for sewage disposal  
services rendered to customers of the Cedar Creek Sewer Company,  
Inc., located within its service area.

Type of Service Rendered

Monthly Charge

Single-Family Residence

\$10.55 per Residence